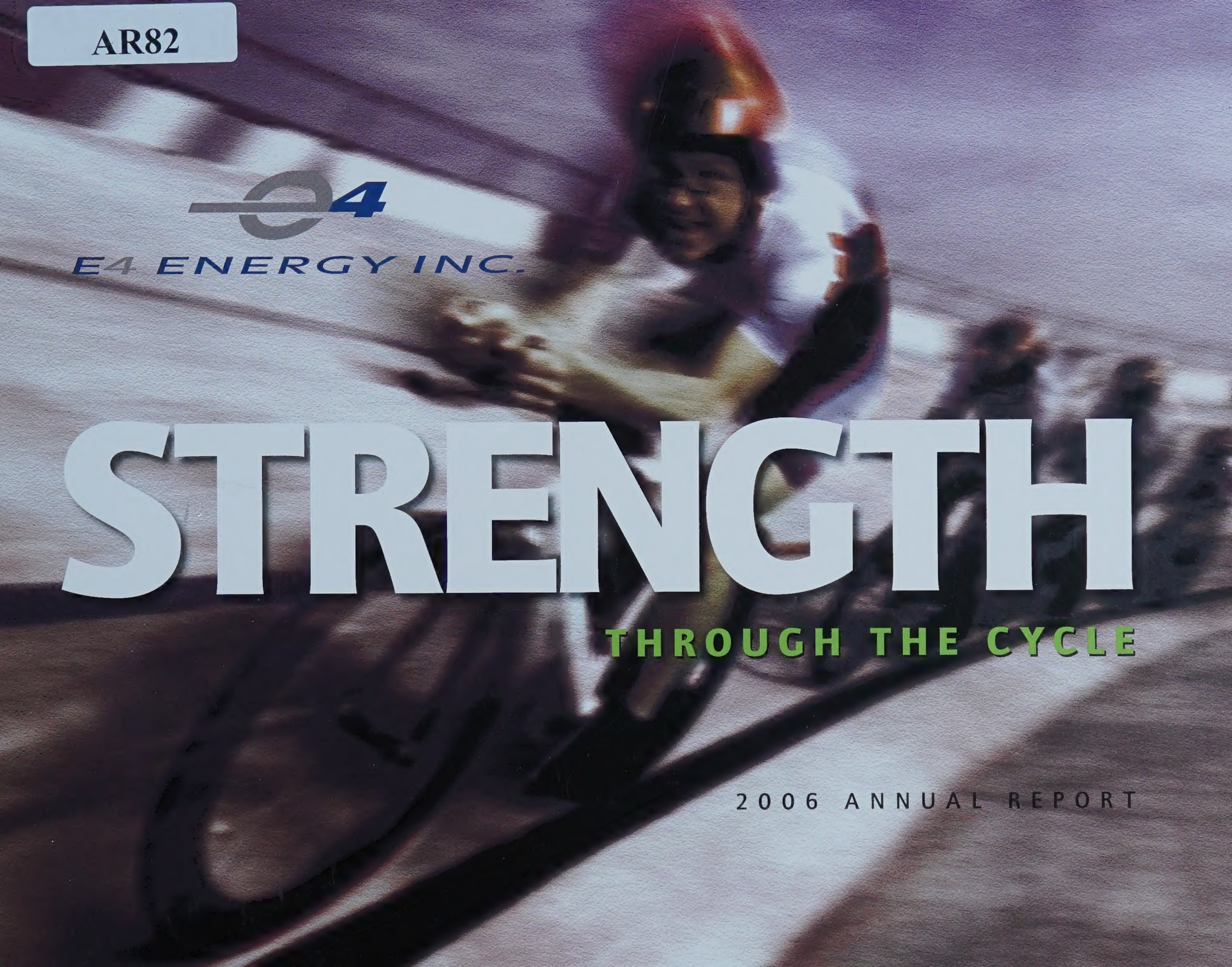
E4 ENERGY INC.

STRENGTH

THROUGH THE CYCLE

2006 ANNUAL REPORT



E4 ENERGY INC.

Profile

E4 Energy Inc. is a junior oil and natural gas exploration and production company based in Calgary, Alberta. The Company focuses its operations in Northeast British Columbia and in East Central and Southern Alberta. E4 has established a solid foundation for continuous growth by accumulating large landholdings in high-growth-potential areas, closely monitoring its balance sheet and balancing its asset portfolio in terms of risk and commodity mix. The Company was established on August 23, 2005. E4 trades on the TSX Venture Exchange (TSX-V) under the symbol EFE.

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Annual General Meeting

June 6, 2007

E4's annual general meeting will be held at 9 a.m. (Mountain Daylight Time) on June 6 in Great Room 3 of the Sandman Inn, 888 7th Ave S.W., Calgary, Alberta. Shareholders are encouraged to attend. Those unable to attend should complete and return the form of proxy.

Internally generated prospects

- Invested extensively in land in 2006
- Avoided high-priced corporate acquisitions
- Active drilling program of 27 gross wells with a 96 percent success rate
- Grass roots full-cycle play generation

Capital management

- Clean balance sheet with low debt
- Solid cash flow stream to help fund capital expenditures
- Declining operating costs delivering maximum netbacks
- Monitoring capital allocations frequently to maintain financial integrity

Operating approach

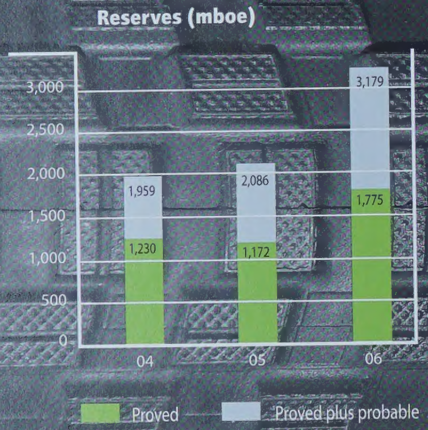
- High working interests (average 78 percent in Q1 2007) and operatorship (90 percent of production) for maximum control and efficiency
- Majority of infrastructure Company-owned and operated
- A balanced strategy for achieving long-term growth
- Primarily shallow- to medium-depth oil and natural gas targets, with multi-zone potential

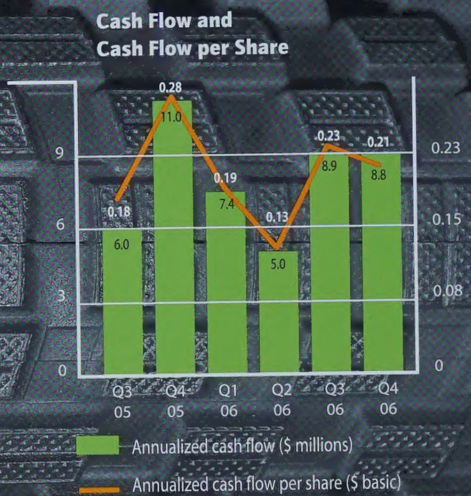
Production (boe/d)
Production per Share (boe/d per million shares)

Steady growth

E4 has achieved 100 percent drillbit-driven production growth since its inception. Through careful capital management, overall volume growth has translated into production growth on a per share basis.

Building through the cycle in 2007 and beyond


Reserves (mboe)
3,000
2,500
2,000
1,500
1,000
500
0
1,959
1,230
2,086
1,172
3,179
1,775
04
05
06
Proved
Proved plus probable


Cash Flow and
Cash Flow per Share
9
6
3
0
0.23
0.15
0.08
0
0.18
6.0
0.28
11.0
0.19
7.4
0.13
5.0
0.23
8.9
0.21
8.8
Q3 05
Q4 05
Q1 06
Q2 06
Q3 06
Q4 06
Annualized cash flow ($ millions)
Annualized cash flow per share ($ basic)


Undeveloped Land (Net Acres)
and Total Land (Gross Acres)
100,000
75,000
50,000
25,000
73,000
37,000
95,700
48,900
112,400
63,200
125,200
76,600
129,500
79,400
128,500
75,600
Q3 05
Q4 05
Q1 06
Q2 06
Q3 06
Q4 06
Undeveloped land (net acres)
Total land (gross acres)

Corporate Highlights

The financial data presented has been presented in accordance with GAAP. The reporting and the measurement currency is the Canadian dollar.

	2006 Q4	2006 Year Ended	2005 Q4	2005 Year Ended	2004 Q4	2004 Year Ended
Operational Results						
Production						
Natural gas (mcf/d)	4,086	3,346	2,848	2,465	1,694	1,420
Crude oil and NGL (bbls/d)	371	302	248	319	376	246
Total production (boe/d)	1,052	860	723	730	658	483
Average realized pricing						
Natural gas ($/mcf)	7.38	6.89	12.28	9.57	7.09	6.64
Crude oil ($/bbl)	55.36	64.15	67.63	64.77	55.76	51.00
Combined average ($/boe)	48.20	49.33	71.61	60.56	50.26	45.57
Selected Financial Results *($ thousands except per share)*						
Petroleum and natural gas revenue	4,665	15,486	4,768	16,202	3,049	8,055
Royalties	852	2,869	880	2,750	270	645
Operating expenses and transportation	1,088	3,379	774	3,356	612	1,804
General and administrative expenses	505	2,433	775	2,685	436	1,645
Funds generated from operations [1]	2,191	7,502	2,752	7,708	1,484	3,465
Basic per share	0.05	0.19	0.07	0.28	0.07	0.16
Diluted per share	0.05	0.19	0.07	0.28	0.07	0.16
Cash flow from operating activities	2,862	6,847	2,161	5,694	2,707	3,238
Depletion, depreciation and accretion expense	2,838	9,433	2,254	7,363	1,336	6,038
Net earning (loss) before discontinued operations	(347)	(119)	409	304	832	(1,820)
Basic per share	(0.01)	(0.00)	0.01	0.01	0.04	(0.08)
Diluted per share	(0.01)	(0.00)	0.01	0.01	0.04	(0.08)
Net earnings (loss)	(347)	(119)	409	304	818	(1,956)
Basic per share	(0.01)	(0.00)	0.01	0.01	0.04	(0.09)
Diluted per share	(0.01)	(0.00)	0.01	0.01	0.04	(0.09)
Capital spending	4,482	23,543	4,458	10,912	4,837	11,365
Total assets (end of period)	68,305	68,305	52,741	52,741	36,041	36,041
Total debt and working capital deficiency (surplus)	9,649	9,649	796	796	12,281	12,281
Shareholders' Equity	47,103	47,103	40,446	40,446	15,396	15,396
Common shares outstanding *(thousands)*	42,644	42,644	38,671	38,671	22,577	22,577

[1] Funds generated from operations is a non-generally accepted accounting principles measure. For E4's calculation of funds generated from operations, refer to Management's Discussion and Analysis.

President's Message

By establishing ourselves in high-growth-potential areas and remaining flexible to take advantage of opportunities arising from recent market volatility, E4 demonstrated strength through the cycle.

In 2006, E4 focused on assembling the land and production base needed to grow the Company over the next number of years. Unlike many juniors, E4 did not work towards maturing its assets for sale to a trust in the near term. Instead, we created per share growth by building upon the previous year's activities, assembling the elements needed to generate future growth and, thereby, making strides towards our long-term goal of becoming a 5,000-10,000 boe/d exploration and production company.

We are a full-cycle exploration company with a business plan to be sustainable through the commodity price cycle. I believe E4 has the key elements it needs to implement this business plan and reach its longer-term production goal. E4 has a highly qualified management team with strong technical abilities and a track record of profitably growing previous junior E&P companies. E4 has a balanced drilling risk profile and well-rounded asset base, producing both natural gas and crude oil. We also have a flexible business model that is easily adaptable to ongoing changes in our business environment.

Our ability to take advantage of opportunities arising from changes in the marketplace has been integral to our success, especially in 2006. Over the past year, Canada's oil and natural gas exploration and production industry went through a period of significant change, more so than in the previous several years. Throughout the commodity price shifts and the unwelcome tax announcement at the end of October, we invested our shareholders' capital in the areas we believed offered the highest long-term growth potential, but that were the most advantageously priced in the current environment.

We also avoided excessive exposure to any one play type, maintaining a balanced commodity mix and risk profile. And, very important in a dynamic price environment, we monitored our capital allocations closely and exercised fiscal discipline. By establishing ourselves in high-growth-potential areas and remaining flexible to take advantage of opportunities arising from recent market volatility, E4 demonstrated strength through the cycle.

Drillbit-driven Growth Across a Broad Risk-Reward Spectrum

E4 was founded with a carefully assembled, balanced mix of assets that together would provide a range of risks, rewards and operating outcomes. We obtained assets that would furnish steady production and cash flow and were amenable to improvement through low-risk and

Balanced portfolio

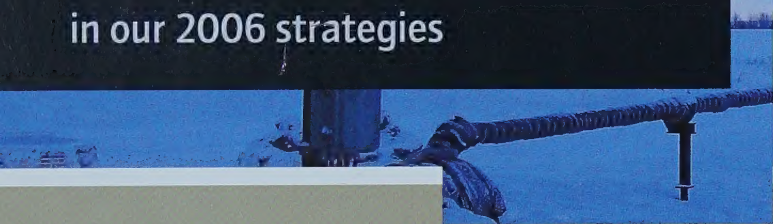
E4 maintains balance in all aspects of its operations. Its three main focus areas are complementary in nature. E4's lower-risk exploitation and development properties in Alberta provide net positive current cash flow for higher-impact, medium-risk exploration, primarily in British Columbia. Reserves remain balanced in terms of oil and natural gas, including CBM.

Flexible business model

E4's flexible business model adjusts its operations to changes in the marketplace. As commodity and land prices fluctuate, E4 allocates its capital accordingly, either by drilling for the currently high-priced commodity or by buying land – whichever delivers the greatest return to shareholders in the long run. E4's flexible approach is made possible by its balanced asset base. Acquisitions are part of the E4 growth model, but E4 has chosen to avoid acquisitions during periods of high asset prices.

Monitoring capital allocations

E4 reviews its balance sheet on a weekly and monthly basis to ensure the Company is never strained on its credit lines. E4 continues to maintain a clean balance sheet. Net debt at year-end 2006 was less than one times 2006 exit annualized cash flow.



Balance, flexibility, discipline

in our 2006 strategies

Going the distance

in 2007 and beyond

Operational efficiency

E4 lowered its operating costs through better cost control and by correcting operational inefficiencies on recently acquired properties. The result of these improvements has been increased commodity netbacks. Even as operating costs for many junior exploration and production companies increased throughout 2006, E4 has cut operating costs in almost every quarter since its founding.

Drillbit-driven growth

E4 will continue to grow its production base through the drillbit. The Company plans to drill 30 wells (24 net) in 2007, spread evenly over its land base in Alberta and British Columbia. Alberta properties typically offer low-risk production additions, while B.C. properties contain higher-risk, higher-reward growth prospects. As in past years, the targets will remain balanced in terms of both risk and commodity.

Internally generated prospects

E4's geological and geophysical team is constantly developing new plays and building E4's prospect inventory. The Company's goal is to continually add production and reserves organically. The additional acres of undeveloped land acquired in 2006 will provide E4's technical team with further opportunities to develop new prospects, with the goal of adding new reserves and production for the next several years.

Our activities in 2006 reflected our chosen risk-reward spectrum, with a weighting towards exploration and development drilling.

low-cost optimization activities, such as well re-entries targeting bypassed pay. Certain properties offered medium-depth opportunities to add measured amounts of oil and natural gas production and reserves through development-oriented drilling. Others were largely undeveloped properties with opportunities for grassroots exploration that could generate material upside with suitably higher capital commitments and technical risks.

E4 thereby created a portfolio of assets with a range of characteristics and opportunities. E4 operates the majority of its projects and owns the majority of the associated infrastructure. We maintain a high average working interest as well as the flexibility to pursue oil or natural gas targets as commodity prices shift.

Our activities in 2006 reflected our chosen risk-reward spectrum, with a weighting towards exploration and development drilling. Overall, E4 achieved steady production growth in 2006, entirely through the drillbit. We focused on drilling activities in the first half of the year when land prices were still inflated, largely due to competition from the income trusts. Our 2006 field program targeted higher-risk, higher-potential-reward oil and natural gas plays in our Northeast British Columbia and East Central Alberta focus areas, accompanied by our first drilling in the new Southern Alberta focus area.

The Company drilled 27 wells (20.85 net) in 2006 at an average 77 percent working interest. Our drilling success rate was 96 percent.

Access to Field Services

The supply shortage and high cost of field services in the year's first half created challenges for nearly all producers. However, E4 continued to have good access to services through its established supplier relationships. These relationships allowed us to secure rigs and services at lower costs and better timing. That being said, service prices were higher than in previous years.

As of Q1 2007, the costs of field services have not retreated from these unsustainable 2006 peaks to the extent we expected; however, access to these services has steadily improved. In this sense, the industry slow-down is a welcome development for the smaller-market-capitalization companies, which typically have the least bargaining leverage with service-providers. E4 expects to see further reductions in field service costs throughout 2007, which should have a direct and beneficial impact on F&D costs.

The E4 team has a common vision of which regions E4 should operate in to maximize its success, and how to grow the Company's shareholder value.

Land Acquisitions

In Q2 2006, land prices dropped sharply along with commodity prices, making land acquisitions temporarily more appealing than drilling activities. E4 took this opportunity to expand its landholdings — the majority at 100 percent working interest — in existing key areas and in new areas with high growth potential. These additional lands provide us with a new exploration and exploitation drilling inventory representing one to two years' field activity.

Last year, E4 acquired small sections of unconsolidated land along drillable prospects in Oak, Teal, Airport and Boundary in British Columbia. In Alberta, conversely, E4 acquired large contiguous sections of land, primarily in the southern parts of the province, based on promising internally generated exploration prospects in the area.

By 2006 year-end, E4 had spent twice its forecast land acquisitions budget and hence doubled its undeveloped land position to 75,600 net acres. The additional expenditures on land were funded from E4's existing, $23.5 million 2006 capital expenditure program by reallocating capital originally slated for drilling. Although this resulted in lower year-end production than expected, E4 believes its land acquisitions better positioned the Company for future growth.

These land acquisitions were in-line with E4's strategy of remaining flexible in order to mitigate the effects of negative events while pursuing unexpected opportunities. Put simply, we make the most of our money by shifting capital from higher-cost to lower-cost categories in response to short-term changes in market conditions. Going forward, E4 will continuously evaluate potential acquisitions, merger candidates, and large farm-ins to gain access to new land areas.

Good Access to Capital

E4 is fortunate to have a strong institutional following and loyal shareholders. When we go to the markets, we find good support, based on the management team's track record of success with previous companies. Consequently, E4's access to capital remains strong, despite industry-wide concerns. We believe in growth through the drillbit, which requires capital. But we believe equally strongly in looking after our Company's balance sheet and, particularly in these uncertain commodity price and market conditions, we monitor and manage those numbers very carefully.

In November 2006, E4 completed a flow-through equity financing to accelerate the Company's drilling programs in December 2006 and the 2007 budget year. Under the bought-deal private placement, E4 issued 3,889,000 flow-through shares at $1.80 per share for gross proceeds of $7,000,200.

E4's ability to pursue growth through drilling or acquisitions, or both, is a key competitive advantage.

Coming out of 2006 we enjoyed a strong financial position, with net debt at less than one times our Q4 annualized cash flow. This means we are well positioned to execute our 2007 capital program, which will continue our focus on growth through development of internally generated prospects. Currently, we do not have plans to raise new equity this year.

Management Team

All of E4's management team and employees have worked and enjoyed past successes together. Our management team has a strong technical background, decades of combined experience and an enviable track record of generating prospects in the Western Canada Sedimentary Basin (WCSB) – and drilling them successfully. The E4 team has a common vision of which regions E4 should operate in to maximize its success, and how to grow the Company's shareholder value.

2007 Outlook

E4 is in a good position for continued growth in 2007. We have a strong balance sheet, a good production base of 1,050 boe/d coming out of 2006, a two-year prospect inventory balanced by risk and commodity, and a large undeveloped land base. E4 expects to continue operating with the same overall focus as in 2006. Amid continued price volatility and the industry's leaner overall access to capital, we will monitor our balance sheet and the business environment to invest our shareholders' capital wisely.

A welcome development that we observed in the early months of 2007 was the increase in opportunities to acquire land or companies. There are more available now than there have been for the last several years, because of reduced competition from the income trusts. We believe the continued volatility in commodities markets will extend this trend. E4 will continue to consider merger and acquisition opportunities that complement its asset portfolio and further its business strategy. We expect the majority of our growth, however, will come from drilling the home-grown prospect inventory identified by our strong, experienced exploration team. E4's ability to pursue growth through drilling and acquisitions, or both, is a key competitive advantage.

The Company's enviable home-grown drilling inventory of more than 60 locations provides geographical diversification, a balanced risk-reward profile and a workable commodity mix given today's pricing.

2007 Capital Program and Guidance

The Company's enviable home-grown drilling inventory of more than 60 locations provides geographical diversification, a balanced risk-reward profile and a workable commodity mix given today's pricing. E4's 2007 capital program will finance drilling approximately 30 wells (24 net) at a continued high average working interest of 80 percent.

The year's drilling locations are spread evenly throughout Alberta and B.C. and are targeting low- to medium-risk oil and natural gas, including CBM. Drilling and completions expenditures are expected to be approximately $9.5 million, a higher ratio than last year. Field facilities, equipment and optimization projects are expected to cost $6.5 million, and $3.4 million has been allocated to land and seismic. E4 developed its budget with moderate commodity price assumptions of Cdn$7.50 per mcf of AECO natural gas and US$60.00 per barrel of WTI oil.

With this base capital budget of $20 million and a higher planned well-count than in 2006, E4 will have another very active year. Based on the currently planned program, E4 expects to grow production to an average of 1,450 boe/d in 2007, weighted 60 percent to natural gas. Our exit rate should grow to approximately 1,600 boe/d, providing year-over-year production growth of nearly 60 percent. Our capital budget will be financed with projected cash flow of $15 million from operations plus a portion of our bank credit facilities. At present, E4 does not foresee the need for additional financings.

In closing I would like to sincerely thank everyone at E4 and their supportive and encouraging families, both in the field and the office, as well as our shareholders. I would also like to extend my sincere thanks to our Board of Directors for their sound advice and contribution towards achieving E4's vision.

On behalf of the Board of Directors,

Paul C. Starnino
President, Chief Executive Officer and Director

March 30, 2007

Exploration and Operations Review

Discovering upside in our focus areas

E4's balanced asset portfolio and flexible business model allow it to take advantage of a changing marketplace.

E4's exploration strategy in 2006 demonstrated its balanced approach to growing production and its responsiveness to market forces. Last year's field program targeted medium-risk, high-potential-reward oil and natural gas plays primarily in British Columbia. Alberta drilling targets were mainly lower-risk development and exploitation oil and natural gas prospects at medium depths. E4 operates the majority of its projects, including owning area infrastructure. All of its drilling targets and exploration prospects were internally generated.

In the first half of 2006, E4 concentrated on drillbit-driven growth. The Company drilled 27 gross (21.4 net) wells. E4's field successes delivered a 96 percent drilling success rate, and drove its exit production rate to 1,052 boe/d, weighted 60 percent to natural gas.

Land Acquisitions

Strengthening E4's position

Land prices dropped sharply in 2006 along with commodity prices, while field service costs remained high. This made land acquisitions more strategically advantageous than drilling. E4 took advantage of this opportunity and more than doubled its landholdings in existing key areas and in new areas. By Q1 2007 E4 had built its land base to 128,400 gross acres at an average working interest of 72 percent. This foundational activity will help E4 achieve future growth in reserves and production.

KEY PROPERTIES

- Airport
- Laprise
- Greater Fort St. John
- Boundary

East Central Alberta

KEY PROPERTIES

- Provost East/Metiskow
- Greater Richdale
- W4M Coalbed Methane

Southern Alberta

KEY PROPERTIES

- Fincastle
- Cherry
- Province
- Smith Coulee

751
boe/d December 2006 production

31,050
net undeveloped acres

+90
percent operatorship

8
wells planned for drilling in 2007

329
boe/d December 2006 production

8,070
net undeveloped acres

+90
percent operatorship

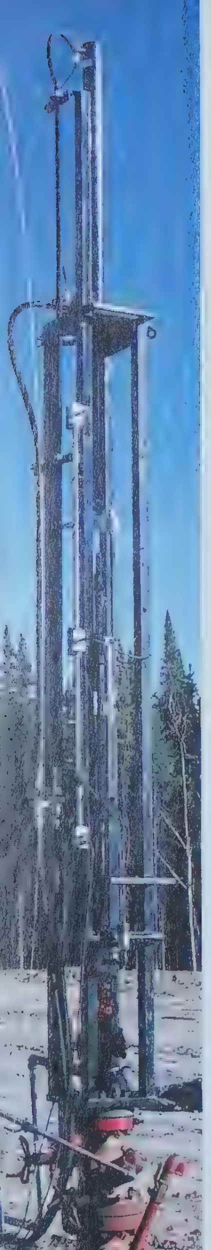
15
wells planned for drilling in 2007

0
boe/d December 2006 production

32,508
net undeveloped acres

+80
percent operatorship

7
wells planned for drilling in 2007



Northeast British Columbia

Airport

Airport has been E4's best growth area to date. Production more than doubled in 2006 to 490 boe/d of natural gas and NGL at year-end, exceeding E4's growth forecast by more than 20 percent. Airport holds further growth opportunities in currently producing horizons plus bypassed pay zones. Airport is a true multi-zone area with natural gas potential from at least seven productive intervals down to 2,000 metres. The majority of E4's area production currently comes from the Halfway and Bluesky zones.

In Q2 2006, E4 drilled a new pool discovery on a seismically defined prospect. The discovery well identified four other potential horizons. With extensive 3-D seismic coverage over 10,000 net acres of tightly held undeveloped lands, E4 sees significant upside through exploration drilling. Five new drilling prospects have been identified to date, with two or more new wells planned for 2007: one step-out from the discovery well and one well targeting a potential bypassed pay zone.

Laprise

E4 sees medium-impact growth potential through development of known producing horizons on this property, which includes 8,000 net acres of undeveloped lands. Regulatory restrictions to date have delayed development, but E4 is hopeful that these will be lifted. The Company's two Charlie Lake/Coplin oil pools were producing 300 boe/d of light oil plus natural gas. E4 operates one pool; the other is non-operated.

E4 has identified several exploration targets, with drilling/recompletion opportunities at depths of less than 1,400 metres. E4 is also in the process of assembling a new natural gas play at Laprise, which may be tested later in 2007.

Greater Fort St. John

Greater Fort St. John includes the Teal, Oak and Lagarde properties, none of which has significant production at present. These properties together hold multiple drill-ready prospects in eight identified target zones, any of which could have a significant impact on E4. Within E4's asset portfolio mix, Greater Fort St. John fills the less-developed, grass roots, higher-risk, higher-reward-potential category. All properties here are held at 100 percent working interest. In 2006, E4 added a number of concentrated but prospective "rifle shot" land holdings, bringing its land base to 12,210 undeveloped acres at year-end.

Greater Fort St. John's multi-zone targets can hold quite prolific light crude oil and natural gas pools. Gas deliverability can be 0.5-3 mmcf/d, while oil pools may yield reserves of 100,000-300,000 bbls per successful well. No drilling occurred in 2006, but in Q1 2007 E4 re-entered a well at Lagarde. Results were successful, and the re-entry well is expected to be tied-in by late Q2. Backed by extensive 3-D and 2-D seismic, E4 has four exploratory prospects at Teal and Oak that it intends to drill in 2007. The Company has identified several follow-up locations that may be drilled if these wells are successful.

Boundary

E4 drilled two 100 percent working interest wells on its 1.5 sections of land in the Boundary area in December 2006. The first well discovered a new oil pool and is presently producing at 70 bbls/d, while the second well tested the limits of the same pool and was dry. The Company has three follow-up locations identified, with plans to develop this pool later this year.

Airport

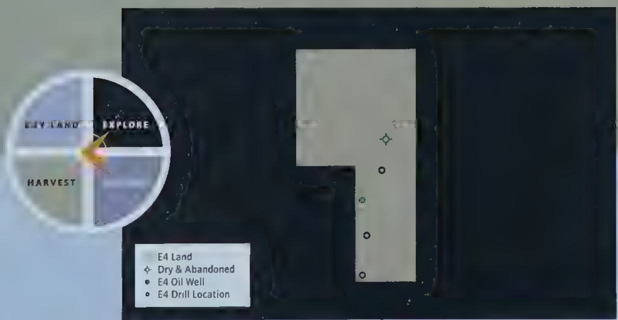
Multi-zone natural gas potential – growth more than doubled in 2006

Laprise

Two producing light-oil pools, exploration and development potential

Boundary

2006 oil discovery, lower-risk development potential



Greater Fort St. John

Grass roots exploration play with multi-zone, high-impact natural gas and light oil prospects

British Columbia Properties

E4's British Columbia properties provide a broad range of higher-impact, higher-potential-reward exploration and development prospects from multiple zones at shallow to medium depths. E4's internally generated drilling program increased production by 71 percent during 2006, and by Q1 2007 the B.C. assets were averaging 670 boe/d, weighted 75 percent to natural gas. E4 holds a 75 percent average working interest and operates more than 90 percent of its B.C. assets. The Company holds 31,050 net undeveloped acres in the province. For 2007 E4 has a drilling program of 10 wells underway and planned.

Alberta

Metiskow (Provost West)

Since farming-into this area late in 2005 E4 has grown the Provost properties into its largest production source in Alberta. Metiskow is a solid provider of cash flow, funding E4's higher-impact exploration elsewhere. E4's farm-in commitment included three wells. As part of the farm-in commitment, two wells were drilled at Metiskow, which were successful and came on-production in early 2006. The water-handling facility in the area provides a competitive edge that holds down operating costs of the area's medium-depth, medium-gravity oil pools. Extensive 3-D seismic coverage provided another advantage as E4 initiated infill drilling. In total for 2006 the Company drilled 11 (6 net) development wells, adding 140 boe/d of net production. Another infill well was drilled in Q1 2007, the first of up to five further infill wells planned for the year.

Provost East

After re-evaluation of existing 3-D seismic data E4's third farm-in commitment well discovered a new Dina oil pool in January 2006. Following this drilling success E4 purchased additional land at 100 percent working interest in a neighbouring, abandoned Dina oil pool. These pools can be prolific, with more than 1 million bbls of recoverable oil each. E4's vertical discovery well encountered thicker than average net pay, making the pool a strong candidate for horizontal development.

Provost East is unquestionably a growth property. In 2006 two horizontal wells were drilled and are currently producing at restricted rates pending the completion of a water handling facility. The key is to gain access to a water-handling facility in advance of development drilling, either on-site or through pipeline access, to reduce operating costs and achieve favourable netbacks. In Q1 2007 the Company was finalizing an agreement concerning water handling. Once this is in place, horizontal development drilling will follow, and production additions by year-end could be material.

Greater Richdale

Greater Richdale is a solid "bread-and-butter" area that provides stable production and cash flow with low-risk optimization and exploitation drilling opportunities. Activities in 2006 were limited to drilling one natural gas well and shooting two 3-D seismic programs, as E4 redeployed capital into land acquisitions. Greater Richdale's production was solid in 2006, and exit volumes were 85 boe/d. With 10,000 net acres of undeveloped land and year-round access, Greater Richdale continues to hold opportunities. Multiple available horizons include the Edmonton, Belly River, Mannville and Banff. E4 plans to drill up to four wells here in 2007. Greater Richdale is also the scene of E4's coalbed methane play, described below.

Southern Alberta

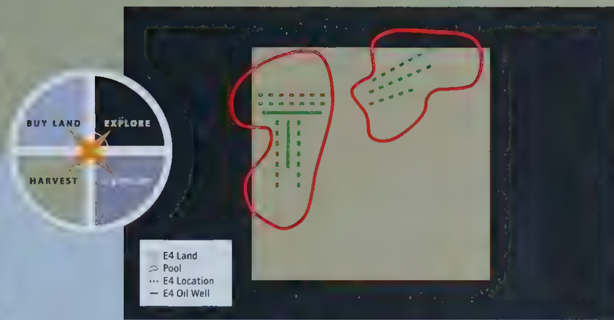
E4's southern Alberta tight gas play is emerging as a potential new core area, based on grassroots work in an under-explored niche within Alberta's vast shallow gas region. Just one year ago E4 had no land or production here. The Company's calculated approach included exploratory drilling of the Medicine Hat, Milk River and Second White Specks potential, followed by an extensive land acquisition program (part of E4's 2006 capital redeployment). Five of six 100 percent E4 wells were successful, after which E4 accumulated 64 sections of land, most at 100 percent working interest. Further drilling is planned in 2007 on a large inventory with multiple locations.

Coalbed Methane (CBM)

E4's CBM play is targeting Alberta's extensive Horseshoe Canyon dry coals. In 2006, E4 re-entered two old wells, which were put on production at rates of 125 mcf/d each (water-free). E4 ramped up activities in Q1 2007, drilling six successful new CBM wells that were tied-in in April. Three further CBM wells are planned before year-end.

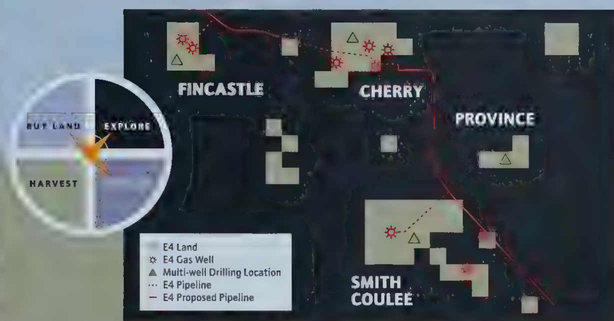
Metiskow (Provost West)
Low-risk infill drilling to add production volumes

Provost East
Dina oil pool discovery, strong reserves potential



Greater Richdale
Steady production and cash flow, low-risk opportunities

Southern Alberta
Emerging new core area – tight, shallow natural gas



Alberta Properties

In addition to providing steady, low-risk cash flow, E4's Alberta properties are yielding exciting new discoveries with a lot of upside and significant growth potential. E4's Alberta production totalled 370 boe/exiting 2006. The Company holds more than 44,000 net undeveloped acres, concentrated in east-central and southeast Alberta. With several recent oil and natural gas discoveries, E4's drilling/recompletions inventory in Q1 2007 totalled more than 45 locations.

Management's Discussion and Analysis

The following discussion and analysis as provided by the management of E4 Energy Inc. ("E4" or "the Company") as of April 12, 2007, is to be read in conjunction with the audited financial statements and related notes for the years ended December 31, 2006 and 2005, all of which were prepared in accordance with Canadian generally accepted accounting principles (GAAP). The reporting and the functional currency is the Canadian dollar, except as noted.

Description of Company – E4 Energy Inc., formerly known as Southpoint Resources Ltd., is an independent, emerging crude oil and natural gas company actively engaged in the exploration for, development and production of natural gas and crude oil reserves in Alberta and British Columbia, Canada. The Company is subject to the provisions of the Alberta Business Corporations Act and its common shares are publicly listed and traded on the TSX Venture Exchange under the symbol EFE.

Non-GAAP Measures – The MD&A contains the term "funds generated from operations" and "netbacks", both of which are non-GAAP terms. The Company uses these measures to help evaluate its performance. Management considers netbacks an important measure as it demonstrates its profitability relative to current commodity prices. Management uses funds generated from operations to analyze operating performance and leverage and considers funds generated from operations to be a key measure as it demonstrates the Company's ability to generate the cash necessary to fund future capital investments and to repay debt. Funds generated from operations should not be considered an alternative to, or more meaningful than, cash flow from operating activities as determined in accordance with GAAP as an indicator of the Company's performance. Therefore, references to funds generated from operations or funds generated from operations per share (basic and diluted) may not be comparable with the calculation of similar measures by other entities. All references to funds generated from operations throughout this report are based on cash flow from operating activities before changes in non-cash working capital. Funds generated from operations per share are calculated using the basic and diluted weighted average number of shares for the period.

Boe Presentation – Barrels of oil equivalent (boe) may be misleading, particularly if used in isolation. A boe conversion ratio of six thousand cubic feet (mcf) to one barrel (bbl) is based on an energy equivalency conversion method primarily applicable at the burner tip and is not intended to represent a value equivalency at the wellhead. All boe conversions in this report are derived by converting natural gas to oil in the ratio of 6 mcf of natural gas to 1 bbl of oil.

Forward-Looking Information – Statements throughout this MD&A that are not historical facts may be considered "forward-looking statements". These forward-looking statements sometimes include words to the effect that management believes or expects a stated condition or result. Forward-looking statements included in the MD&A concern anticipated production and capital expenditures.

Forward-looking statements and information are based on the Company's current beliefs as well as assumptions made by and information currently available to the Company concerning anticipated financial performance, business prospects, strategies and regulatory developments. Although management considers these assumptions to be reasonable based on information currently available to it, they may prove to be incorrect.

By their very nature forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks that predictions, forecasts, projections and other forward-looking statements will not be achieved. E4 cautions readers not to place undue reliance on these statements as a number of important factors could cause the actual results to differ materially from the beliefs, plans, objectives, expectations and anticipations, estimates and intentions expressed in such forward-looking statements. These factors include, but are not limited to: the volatility of oil and gas prices; production and development costs and capital expenditures; the imprecision of reserve estimates and estimates of recoverable quantities of oil and gas reserves; environmental claims and liabilities; incorrect assessments of value when making acquisitions; increases in debt service charges; the loss of key personnel; the marketability of production; defaults by third-party operators; fluctuations in foreign currency and exchange rates; inadequate insurance coverage; compliance with environmental laws and regulations; changes in tax laws; and the Company's ability to access external sources of debt and equity capital.

The Company cautions that the foregoing list of factors that may affect future results is not exhaustive. When relying on the Company's forward-looking statements to make decisions with respect to the Company, investors and others should carefully consider the foregoing factors and other uncertainties and potential events. The forward-looking statements and information contained in this MD&A are as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws.

CREATION OF E4 ENERGY INC.

Naneco Minerals Ltd. was continued under the laws of the Province of Alberta and changed its name to Southpoint Resources Ltd. on February 6, 2002. Southpoint at that time refocused its efforts to the exploration and development of petroleum and natural gas in western Canada. On August 24, 2005, the Company changed its name to E4 Energy Inc. in conjunction with the business combination discussed in Note 3 to the audited consolidated financial statements for the year ended December 31, 2006.

Management's Discussion and Analysis

SELECTED QUARTERLY INFORMATION

The financial data presented below has been presented in accordance with GAAP with the exception of funds generated from operations. The reporting and the measurement currency is the Canadian dollar.

	2006				2005			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Operational Results								
Production								
Natural gas (mcf/d)	4,086	3,352	2,766	3,171	2,848	2,248	2,280	2,481
Crude oil and NGL* (bbls/d)	371	346	214	275	248	249	296	486
Total production (boe/d)	1,052	905	675	804	723	624	676	900
Average realized pricing								
Natural gas ($/mcf)	7.38	6.10	6.15	7.74	12.28	9.79	7.47	8.18
Crude oil ($/bbl)	55.36	70.30	68.94	64.74	67.63	71.78	63.01	60.72
Combined average ($/boe)	48.20	49.45	47.08	52.68	71.61	63.95	53.18	55.46
Selected Financial Results *($ thousands except per share)*								
Petroleum and natural gas revenue	4,665	4,117	2,892	3,812	4,768	3,670	3,271	4,493
Royalties	852	656	521	840	880	592	550	728
Operating expenses and transportation	1,088	858	667	766	774	676	890	1,016
General and administrative expenses	505	462	714	752	775	968	523	419
Funds generated from operations	2,191	2,221	1,252	1,838	2,752	1,500	1,144	2,312
Cash flow from operating activities	2,862	479	834	2,672	2,161	2,598	(1,633)	2,568
Depletion, depreciation and accretion expense	2,838	2,433	1,875	2,287	2,254	1,563	1,506	2,040
Net earnings (loss)	(347)	173	826	(771)	409	(310)	(422)	627
Basic per share	(0.01)	0.00	0.02	(0.02)	0.01	(0.01)	(0.02)	0.03
Diluted per share	(0.01)	0.00	0.02	(0.02)	0.01	(0.01)	(0.02)	0.03
Capital spending	4,482	3,617	7,848	7,596	4,458	2,310	871	3,273
Total debt and working capital deficiency	9,649	13,952	12,694	6,337	796	9,289	12,992	13,365
Shareholders' equity	47,103	40,543	40,006	38,557	40,446	29,067	15,304	15,653
Common shares outstanding (thousands)	42,644	38,755	38,755	38,755	38,671	33,624	22,577	22,577

**natural gas liquids*

Petroleum and Natural Gas Production

E4's production for the year ended December 31, 2006 averaged 860 boe/d. The production was comprised of 302 bbls/d of crude oil and natural gas liquids (NGL) and 3,346 mcf/d of natural gas. This compares with yearly production for the year ended December 31, 2005 of 730 boe/d, split between crude oil and NGL of 319 bbls/d and natural gas of 2,465 mcf/d. The 18 percent increase in total production was due in large part to a successful drilling program in the Airport area of British Columbia.

In Q4 2006, production averaged 1,052 boe/d, an increase of 46 percent from Q4 2005 when production averaged 723 boe/d. Q4 2006 crude oil and NGL production was 371 bbls/d, compared to Q4 2005 production of 248 bbls/d. Natural gas production, meanwhile, was 4,086 mcf/d in Q4 2006 and 2,848 mcf/d in the same period of 2005. These production increases were due to new production from the Airport area of British Columbia and the Provost area of Alberta.

The following table highlights E4's production by reporting period:

	Average Daily Production		
	Natural Gas (mcf/d)	Crude Oil and NGL (bbls/d)	Total (boe/d)(6:1)
Q1 2006	3,171	275	804
Q2 2006	2,766	214	675
Q3 2006	3,352	346	905
Q4 2006	4,086	371	1,052
Year 2006	3,346	302	860
Q1 2005	2,481	486	900
Q2 2005	2,280	296	676
Q3 2005	2,248	249	624
Q4 2005	2,848	248	723
Year 2005	2,465	319	730

Revenue and Commodity Pricing

E4's petroleum and natural gas revenue for 2006 (before royalties) totalled $15.5 million, comprised of natural gas sales of $8.4 million and crude oil and NGL revenue of $7.1 million. This compares with total revenues of $16.2 million for 2005, which consisted of $8.7 million of natural gas sales and $7.5 million of crude oil and NGL sales. The 4 percent decrease from 2005 to 2006 is due to substantially lower natural gas prices throughout 2006, largely offset by E4's production increases.

During Q4 2006, E4 recorded total revenue before royalties of $4.7 million, consisting of $1.9 million of crude oil and NGL sales and $2.8 million of natural gas sales. This represents a 2 percent decrease from the Q4 2005 total revenue of $4.8 million, which consisted of $3.2 million of natural gas sales and $1.6 million of crude oil and NGL sales. Although E4's average daily production was higher in Q4 2006 than in Q4 2005, this increase was offset by lower commodity prices in Q4 2006, resulting in revenues that were virtually unchanged for the respective periods.

Management's Discussion and Analysis

There were no outstanding derivative instruments to hedge future commodity prices during the years ended December 31, 2006 and December 31, 2005. However, the Company has put into place a fixed price natural gas sales contract for 1,500 gigajoules per day commencing in April 2007.

The following table highlights the composition of E4's revenue before royalties by reporting period:

($ thousands)	Natural Gas	Crude Oil and NGL	Total
Q1 2006	2,210	1,602	3,812
Q2 2006	1,549	1,343	2,892
Q3 2006	1,880	2,237	4,117
Q4 2006	2,776	1,889	4,665
Year 2006	8,415	7,071	15,486
Q4 2005	3,223	1,545	4,768
Year 2005	8,658	7,544	16,202
Year 2004	3,451	4,604	8,055

The following table highlights E4's corporate realized wellhead prices and industry benchmark prices:

	2006 Quarterly Comparison				Year	Year
	Q4	Q3	Q2	Q1	2006	2005
E4 prices:						
Natural gas ($/mcf)	7.38	6.10	6.15	7.74	6.89	9.57
Crude oil and NGL ($/bbl)	55.36	70.30	68.94	64.74	64.15	64.77
Combined ($/boe)	48.20	49.45	47.08	52.68	49.33	60.56
WTI oil at Cushing, Oklahoma (US$/bbl)	60.21	70.55	70.70	63.48	66.24	56.62
Edmonton Par light oil ($/bbl)	64.48	79.17	78.60	69.11	72.84	68.22
Bow River medium oil ($/bbl)	45.69	59.06	62.16	51.29	54.55	44.40
WTI - Lloyd blend differential (US$/bbl)	21.31	19.08	17.16	10.26	16.95	21.41
Nymex Henry Hub natural gas (US$/mmbtu)	6.61	6.52	6.83	9.10	7.26	8.55
AECO natural gas – monthly index ($/mcf)	6.31	5.98	6.22	9.23	6.92	8.42
Currency Exchange rate (US$:Cdn$)	0.878	0.892	0.891	0.866	0.882	0.824

Petroleum and Natural Gas Royalties

The Company incurred an effective royalty rate of 18.5 percent in 2006. This royalty rate, net of the Alberta Royalty Tax Credit (ARTC), compares with a rate of 17 percent for 2005. This slight increase is due to adjustments pertaining to prior periods that were first recognized in the first quarter of 2006. In total dollars, E4 incurred royalties of $2.9 million in 2006 and $2.8 million in 2005.

E4's petroleum and natural gas royalties for Q4 2006 amounted to $0.9 million, identical to the same period of 2005. As a percentage of gross revenue, E4's corporate royalty rate was 18.2 percent for the fourth quarter of 2006 and 18.5 percent for the same period of 2005. On a go-forward basis, E4 expects a slightly higher royalty rate due to the Alberta government's elimination of the ARTC effective January 1, 2007.

The following table highlights E4's effective royalty rates:

	2006 Quarterly Comparison				Year	Year
($ thousands except per unit and royalty rate)	Q4	Q3	Q2	Q1	2006	2005
Crown, net of ARTC	763	588	444	670	2,465	2,282
Freehold and overriding	89	68	77	170	404	468
Total	852	656	521	840	2,869	2,750
Per unit ($/boe)	8.81	7.87	8.48	11.61	9.14	10.32
Effective royalty rate (%)	18.2%	15.9%	18.0%	22.0%	18.5%	17.0%

Operating Expenses

E4 reported field operating costs of $9.21 per boe for the year ended December 31, 2006. This was slightly lower than the average operating costs of $9.49 per boe for the year ended December 31, 2005 and was a result of management's implementation of programs to reduce operating costs such as negotiating more favourable contract operating fees. In total dollars, E4 reported field operating costs of $2.9 million for the year ended December 31, 2006 compared to $2.5 million for the prior year.

In Q4 2006, E4 reported field operating costs of $9.85 per boe. This was 2 percent higher than in the same period of 2005, and the increase is attributable to several compressor repairs that occurred in Q4 2006. In total dollars, E4 incurred field operating costs of $1.0 million in Q4 2006 compared to $0.6 million for the same period of 2005. This increase of 49 percent is due to higher overall production in Q4 2006.

	2006 Quarterly Comparison				Year	Year
	Q4	Q3	Q2	Q1	2006	2005
Total ($ thousands)	953	742	563	633	2,891	2,528
Per unit of production ($/boe)	9.85	8.92	9.16	8.76	9.21	9.49

Transportation Expenses

E4 reported transportation costs of $1.55 per boe for the year ended December 31, 2006, compared to $3.10 per boe for the year ended December 31, 2005. The sharp decrease is due to the lower rates being offered by the trucking contractor utilized in 2006 compared to the trucking contractor utilized in 2005. In Q4 2006, E4 reported transportation costs of $1.40 per boe compared to $2.00 per boe for the same period of 2005.

	2006 Quarterly Comparison				Year	Year
	Q4	Q3	Q2	Q1	2006	2005
Total ($ thousands)	135	116	104	133	488	828
Per unit of production ($/boe)	1.40	1.39	1.69	1.83	1.55	3.10

General & Administrative Expenses (G&A)

For the year ended December 31, 2006, total G&A expenses decreased by 9 percent from the same period of 2005. In 2006, E4 reported total G&A expenses of $2.4 million, compared to $2.7 million in 2005. The decrease was due in large part to the absence of severance costs in 2006, versus costs of $0.6 million in 2005. On a per unit of production basis, G&A expenses were $7.75 per boe in 2006 compared to $7.93 per boe in 2005, excluding severance costs related to the P3 business combination.

E4's total G&A expenses for Q4 2006 amounted to $0.5 million or $5.20 per boe of production, compared to $0.8 million or $11.65 per boe for the comparable 2005 period. This sharp decrease is mostly attributable to non-cash stock-based compensation expense. In Q4 2006, E4 recorded stock-based compensation expense net of capitalization of $0.2 million, or $1.64 per boe. This compares to $0.5 million or $6.77 per boe in Q4 2005.

The Company capitalized employee and associated direct overhead costs of its technical personnel in the amount of $0.9 million in fiscal 2006 and $0.2 million in Q4 2006. In comparison, E4 capitalized overhead in the amount of $0.4 million in fiscal 2005 and $0.2 million in Q4 2005. E4 currently employs 11 office personnel, including six technical staff, and engages the services of two consultants on a part-time basis.

	2006 Quarterly Comparison				Year	Year
($ thousands)	Q4	Q3	Q2	Q1	2006	2005
Cash costs	542	426	605	526	2,099	2,287
Capitalized cash costs	(197)	(192)	(274)	(193)	(856)	(417)
Stock-based compensation (net of capitalization)	160	228	383	419	1,190	815
Total	505	462	714	752	2,433	2,685
Per unit ($/boe)						
Cash costs	5.60	5.12	9.84	7.26	6.69	6.43
Severances	–	–	–	–	–	2.15
Capitalized cash costs	(2.04)	(2.31)	(4.46)	(2.66)	(2.73)	(1.56)
Stock-based compensation (net of capitalization)	1.64	2.74	6.24	5.80	3.79	3.06
Total per unit	5.20	5.55	11.62	10.40	7.75	10.08

Financing Charges

In fiscal 2006 the Company recorded total financing charges of $0.5 million, which consisted of interest expense related to the Company's bank facility of $0.42 million and Part XII.6 tax of $0.04 million. For fiscal 2005, the Company recorded $0.7 million in financing charges, consisting of $0.4 million relating to bank borrowing interest charges on its outstanding debt during the period, $0.1 million in accretion relating to subordinated notes and $0.2 million relating to the early retirement of subordinated notes.

In Q4 2006, the Company recorded total financing charges of $0.2 million, relating entirely to interest on the Company's outstanding debt during the period. In Q4 2005, the Company recorded total financing charges of $0.04 million, also relating entirely to interest on the Company's outstanding debt during the period.

	2006 Quarterly Comparison				Year	Year
($ thousands)	Q4	Q3	Q2	Q1	2006	2005
Interest expense, including Part XII.6 tax	189	148	88	35	460	420
Subordinated note accretion	–	–	–	–	–	117
Loss on early retirement of subordinated note	–	–	–	–	–	147
Total	189	148	88	35	460	684

Depletion, Depreciation and Accretion

E4's depletion and depreciation expenses for the year and quarter ended December 31, 2006 amounted to $9.3 million and $2.8 million, respectively. This equated to $29.70 per boe and $29.00 per boe for the respective periods. For the year and quarter ended December 31, 2005, the Company recorded depletion and depreciation expense of $7.3 million and $2.2 million, respectively, or $27.35 per boe and $33.51 per boe, respectively. The entire oil and gas industry has been hit by higher service costs and the high depletion rates are a result of these higher costs.

The Company's accretion expense relating to its asset retirement obligations (ARO) amounted to $0.1 million for the years ended December 31, 2006 and 2005. In Q4 2006 and Q4 2005, the Company reported accretion expense of $0.03 million in each period.

	2006 Quarterly Comparison				Year	Year
($ thousands except per unit)	Q4	Q3	Q2	Q1	2006	2005
Depletion & depreciation	2,807	2,405	1,844	2,264	9,320	7,291
Accretion	31	28	31	23	113	72
Total	2,838	2,433	1,875	2,287	9,433	7,363
Per unit combined ($/boe)	29.33	29.22	30.50	31.61	30.06	27.62

Income and Capital Taxes

The Company currently has approximately $38.8 million in tax pools available for deduction against future taxable income (net of any projected pool usage necessary to offset taxable income for the year ended December 31, 2006). As a result of these tax pools, E4 does not expect to be cash taxable in the foreseeable future.

With respect to E4's future income tax accounting provision for 2006, the Company recorded a future income tax recovery of $3.0 million. The bulk of this recovery includes the impact of a reduction in federal and provincial tax rates in respect of 2006 through 2010 of $0.8 million, and a reduction of tax valuation allowance of $1.4 million.

The following table outlines the approximate tax pools available to the Company at December 31, 2006.

($ thousands)	Access Rate	Amount
Canadian exploration expense (CEE)	100%	5,001
Canadian development expense (CDE)	30%	9,498
Canadian oil and gas property expense (COGPE)	10%	7,696
Undepreciated capital cost (UCC)	25%	11,208
Foreign exploration and development expense (FEDE)	10%	2,094
Non-capital losses	100%	822
Share issue costs	20%	884
Other	20%	1,585
Total tax pools		38,788

Funds Generated From Operations, Cash Flow From Operations and Net Earnings

E4's funds generated from operations totalled $7.5 million for the year ended December 31, 2006. This represents a slight decrease of 3 percent from the $7.7 million in funds generated from operations in 2005. In Q4 2006, the Company's funds generated from operations was $2.2 million, a 21.5 percent decrease from $2.8 million in Q4 2005. The decreases in the 2006 periods from the respective periods in 2005 are due to lower natural gas prices throughout 2006.

The Company reported a net loss of $0.1 million for the year ended December 31, 2006. This compares with net earnings of $0.3 million for 2005. In Q4 2006, E4 reported a net loss of $0.3 million versus net earnings of $0.4 million in Q4 2005. The net losses reported in the respective periods of 2006 compared to the net earnings reported in the same periods of 2005 were due to lower commodity prices, higher depletion, depreciation and accretion and a recovery in future income taxes.

	2006 Quarterly Comparison Q4	Q3	Q2	Q1	Year 2006	Year 2005
Funds generated from operations [1] ($ thousands)	2,191	2,221	1,252	1,838	7,502	7,708
Per share – basic ($)	0.05	0.06	0.03	0.05	0.19	0.28
Per share – diluted ($)	0.05	0.06	0.03	0.05	0.19	0.28
Cash flow from operating activities ($ thousands)	2,862	479	834	2,672	6,847	5,694
Net earnings (loss) ($ thousands)	(347)	173	826	(771)	(119)	304
Per share – basic ($)	(0.01)	0.00	0.02	(0.02)	(0.01)	0.01
Per share – diluted ($)	(0.01)	0.00	0.02	(0.02)	(0.01)	0.01

[1] *Funds generated from operations is a non-GAAP measure and represents cash flow from operations before changes in non-cash working capital.*

Capital Expenditures

E4 incurred capital expenditures of $4.5 million and $23.5 million, respectively, for Q4 2006 and the year ended December 31, 2006. The majority of the capital expenditures incurred was for the drilling of 27 gross wells and land purchases. Outlined below are E4's capital expenditures by category.

($ thousands)	2006 Quarterly Comparison Q4	Q3	Q2	Q1	Year 2006	Year 2005
Land	469	869	1,003	1,771	4,112	1,463
Seismic	36	–	110	1,012	1,158	706
Drilling & completions	3,228	1,191	6,069	3,538	14,026	5,225
Field facilities & equipment	452	1,227	151	805	2,635	2,803
Other [1]	205	193	276	193	867	448
Total cash capital expenditures	4,390	3,480	7,609	7,319	22,798	10,645
Non-cash capitalized stock-based compensation	92	137	239	277	745	267
Total capital expenditures	4,482	3,617	7,848	7,596	23,543	10,912

[1] *Includes office equipment, computer hardware and direct G&A.*

Liquidity and Capital Resources

E4's primary sources of liquidity to fund its exploration and development capital program are the Company's internal funds generated from operations and E4's revolving operating bank credit facility. E4 utilizes this facility to fund daily operating activities and acquisitions as needed. Because of the liquidity and capital resource alternatives available to the Company, including funds generated from operations, E4 believes that its liquidity is sufficient to fund planned spending on exploration and development projects and undeveloped acreage necessary for long-term, profitable growth. The Company anticipates that public capital markets will serve as the principal source of capital to finance any future corporate acquisitions and/or significant property purchases. E4 has issued equity in the past, and expects that this source of capital will continue to be available to the Company in the future to help fund potential acquisitions.

The Company's capital program has been established at $20 million for 2007. Cash provided by operating activities is budgeted to provide a significant portion of the funding for this program. The Company is mindful of the current weakness in Canadian natural gas markets due to seasonal factors and historically high levels of natural gas in storage and re-evaluates its capital program on an on-going basis.

At December 31, 2006, E4 had net debt (bank debt plus/minus working capital) of $9.6 million, 42.6 million common shares outstanding with a carrying amount of $47.5 million and a market capitalization of $52.5 million. In comparison, at December 31, 2005, the Company was capitalized with net debt of $0.8 million, 38.7 million common shares outstanding with a carrying amount of $42.7 million and a market capitalization of $69.6 million. The increase in net debt is attributable to the aggressive capital expenditure program undertaken by E4 in 2006.

As at April 17, 2007, the Company had in-place credit facilities with a major lending institution providing a total borrowing base of $18 million. The bank is expected to conduct its annual credit review in late May 2007.

End of period	2006 Quarterly Comparison				Year	Year
($ thousands)	Q4	Q3	Q2	Q1	2005	2004
Working capital/deficiency (includes cash)	1,724	69	3,058	1,773	796	5,457
Bank debt, subordinated notes and convertible debentures	7,925	13,883	9,636	4,564	–	6,822
Total	9,649	13,952	12,694	6,337	796	12,279
Assets	68,305	66,919	64,049	58,126	52,741	36,041

Common Share Information

		2006 Quarterly Comparison				Year
		Q4	Q3	Q2	Q1	2005
Share price	High	$ 1.51	$ 1.65	$ 1.74	$ 1.85	$ 2.15
	Low	$ 1.05	$ 1.14	$ 1.15	$ 1.36	$ 0.91
	Close	$ 1.23	$ 1.24	$ 1.25	$ 1.42	$ 1.80
Average daily trading volume		48,629	25,408	53,078	58,895	56,150
Common shares	Outstanding at period end	42,643,672	38,754,672	38,754,672	38,754,672	38,671,338
	Weighted average basic	40,107,368	38,754,672	38,754,672	38,752,450	27,557,342
	Weighted average diluted	40,107,368	38,857,173	38,779,801	38,752,450	27,622,879
Stock options	Outstanding at period end	3,209,000	3,209,000	3,240,000	3,240,000	2,748,335
Warrants	Outstanding at period end	–	–	–	667,667	667,667

Contractual Obligations

The Company is committed to contractual obligations and commitments in the normal course of operations and financing activities. These are outlined below:

($ thousands)	1 Year	1-3 Years	4-5 Years	Beyond 5 Years	Total
Operating lease obligations [1]	189	142	–	–	331

[1] Operating lease obligations pertain to the Company's Calgary, Alberta head office lease. In addition to lease amounts, the Company is responsible for it proportionate share of operating costs, which are periodically reviewed and determined by the landlord.

In addition, at December 31, 2006, the Company is committed to incurring approximately $6.4 million prior to December 31, 2007 on qualifying exploration and development expenditures relating to the flow-through financings of November 30, 2006. (See Note 9 (d) to the audited consolidated financial statements at December 31, 2006.)

Risk Management Activities

On January 31, 2007, the Company entered into a firm fixed price agreement with one of its natural gas purchasers. The term of the agreement is such that the first 1,500 gigajoules per day of natural gas production from the Company's McMahon receipt station will have a fixed price of $7.40 per gigajoule. This contract commenced on April 1, 2007 and expires on October 31, 2007.

Off-Balance Sheet Arrangements

The Company did not enter into any off-balance-sheet arrangements during the year ended December 31, 2006.

Related-Party Transactions

A director of the Company is a partner at a law firm that provides legal services to the Company. During the year ended December 31, 2006, the Company paid a total of $50,000 to this firm for legal fees and disbursements. An additional amount of $40,000 was accrued at December 31, 2006 and was subsequently paid in 2007.

Newly Adopted Accounting Policies

There were no significant accounting policies newly adopted during the year ended December 31, 2006.

Financial Instruments

The following standards regarding financial instruments are effective for January 1, 2007: 3855 "Financial Instruments – Recognition and Measurement"; 3861, "Financial Instruments – Disclosure and Presentation"; 1530, "Comprehensive Income"; and 3865, "Hedges". These standards require all financial instruments other than held-to-maturity investments, loans and receivables to be included on a company's balance sheet at their fair value. Held-to-maturity investments, loans and receivables would be measured at their amortized cost. These standards create a new statement for comprehensive income that will include changes in the fair value of certain financial instruments. As a result of these new standards, the Company will not use hedge accounting beginning January 1, 2007 and will record the fair value of its crude oil and natural gas derivative contracts under its risk management program. The Company is currently assessing the impact of these new standards on its financial statements.

Business Risks and Uncertainties

The Company's exploration and development activities are focused in the Western Canada Sedimentary Basin within Alberta and British Columbia, which is characterized as being highly competitive with competitors varying in size from small junior producers to significantly larger, fully-integrated energy companies possessing greater financial and personnel resources. The Company recognizes certain risks inherent in the crude oil and natural gas industry, such as finding and developing oil and natural gas reserves at economic costs, drilling risks, producing oil and natural gas in commercial quantities, environmental and safety risks, and commodity price and political risks and uncertainties. E4 has engaged professional management and technical personnel with many years of experience in the oil and natural gas business to address and prudently manage and mitigate these risks.

Disclosure Control Risks

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by the Company is accumulated and communicated to its management as appropriate to allow timely decisions regarding required disclosure. The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation of the effectiveness of the Company's disclosure controls and procedures as of the date of this MD&A, that disclosure controls and procedures provide reasonable assurance that material information is made known to them by others within the Company. Certain weaknesses, however, have been identified and the Company's Chief Executive Officer and Chief Financial Officer do not expect that the disclosure controls and procedures can prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

Internal Controls Over Financial Reporting

Multilateral Instrument 52-109 of the Canadian Securities Administrators defines internal controls over financial reporting as "a process designed by, or under the supervision of the issuer's chief executive officers and chief financial officers or persons performing similar functions, and enacted by the issuer's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the issuer's GAAP and includes those policies and procedures that:

a) Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer.

b) Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with the issuer's GAAP, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer.

c) Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the issuer's assets that could have a material effect on the annual financial statements or interim financial statements."

The Company has, under the supervision of its Chief Executive Officer and Chief Financial Officer, designed a process for internal control over financial reporting, which process has been enacted by the Company's board of directors and management. The process was designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP and incorporates policies and procedures as described above.

Given the size of the Company, the evaluation of the design of internal controls over financial reporting for the Company resulted in the identification of the following weaknesses:

1) Management is aware that due to its relatively small scale of operations there is a lack of segregation of duties due to a limited number of employees dealing with accounting and financial matters. However, management has concluded that considering the employees involved and the control procedures in place, including management and Audit Committee oversight, risks associated with such lack of segregation are not significant enough to justify the expense associated with adding employees to clearly segregate duties.

2) As part of its business, the Company records complex and non-routine transactions. These transactions can be very technical in nature and the determination of the appropriate accounting for these transactions requires an in-depth understanding of Canadian GAAP. The Corporation's accounting staff has a fair and reasonable knowledge of the rules related to Canadian GAAP and reporting of the transactions may not be recorded correctly, potentially resulting in a material misstatement of the consolidated financial statement of the Company.

   To address this risk, the Company consults with third party-expert advisors on a regular basis for advice and seeks specific advice on proposed or contemplated transactions. The Company would have to considerably increase its size and the scope of its activities before the Company could contemplate having dedicated in-house resources with the required knowledge of all aspects of Canadian GAAP that may impact on the complex and non-routine transactions that the Company may enter into.

There have been no significant changes to the Company's internal control over financial reporting that occurred during the most recent period that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Internal Control Reporting

In March 2006 the Canadian Securities Administrators decided not to proceed with proposed multilateral instrument 52-111, "Reporting on Internal Control over Financial Reporting" and instead proposed to expand multilateral instrument 52-109, "Certification of Disclosure in Issuers' Annual and Interim Filings". The major changes resulting from this are that the Chief Executive Officer and Chief Financial Officer will be required to certify in the annual certificates that they have evaluated the effectiveness of internal controls over financial reporting (ICOFR) as of the end of the financial year and disclose in the annual MD&A their conclusions about the effectiveness of ICOFR. There will be no requirement to obtain an internal control audit opinion from the issuer's auditors concerning management's assessment of the effectiveness of ICOFR. There is also no requirement to design and evaluate internal controls against an external control framework. This proposed amendment is expected to apply for the year ended December 31, 2008. E4 is continuing with its evaluation of ICOFR to ensure it meets the criteria for the proposed certification for December 31, 2008.

Application of Critical Accounting Policies

The preparation of the Company's audited consolidated financial statements in accordance with Canadian GAAP requires E4's management to make estimates, assumptions and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. The basis for these estimates is historical experience and various other assumptions that the Company believes to be reasonable. Actual results could differ from these estimates under different assumptions and conditions.

For further details on the Company's accounting policies, refer to Note 2 to the audited consolidated financial statements for the year ended December 31, 2006.

Full-Cost Accounting

The Company follows the full-cost method of accounting for its crude oil and natural gas operations, whereby all costs related to the exploration for and development of oil and natural gas reserves are capitalized and depleted and depreciated using the unit-of-production method based upon the gross proved petroleum and natural gas reserves as determined by an independent qualified reserve engineering firm. In determining costs subject to depletion, the Company includes estimated future costs to be incurred in developing proved reserves and excludes salvage values and the costs of unproved properties. The costs of acquiring and evaluating unproved properties are excluded from costs subject to depletion until it is determined whether or not proved reserves are attributable to the properties or until impairment occurs.

In applying the full-cost accounting method, a ceiling test is performed to ensure that the capitalized costs are recoverable in the future. Oil and natural gas assets are evaluated in each reporting period to determine whether the carrying amount in a cost centre is recoverable and does not exceed the fair value of the properties in the cost centre. The carrying amounts are assessed to be recoverable when the sum of the undiscounted cash flows expected from the production of proved reserves, the lower of cost and market of unproved properties and the cost of major development projects exceeds the carrying amount of the cost centre. When the carrying amount is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying amount of the cost centre exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves, the lower of cost and market of unproved properties and the cost of major development projects of the cost centre. The cash flows are estimated using expected future product prices and costs and are discounted using a risk-free interest rate. The calculation of undiscounted cash flows in the ceiling test can be significantly impacted by fluctuations in any of these estimates.

Asset Retirement Obligation

The asset retirement obligation is estimated based on existing laws, contracts or other policies. The fair value of the asset retirement obligation requires an estimate of the future costs to abandon and reclaim wells, pipelines and facilities discounted to its present value using the Company's credit-adjusted risk-free interest rate. The liability is adjusted each reporting period to reflect the passage of time, with the accretion charged to earnings. Revisions to the estimated timing of cash flows or to the original undiscounted cost could also result in an increase or decrease to the obligation. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material.

Income Tax Accounting

The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, any income tax liability or asset, as well as any income tax recovery or reduction, may differ from that estimated and recorded by the Company's management.

Management's Report

Management, in accordance with Canadian generally accepted accounting principles and in accordance with the accounting policies disclosed in the notes to the consolidated financial statements, has prepared the accompanying consolidated financial statements of E4 Energy Inc. The financial and operating information presented in this Annual Report is consistent with that shown in the consolidated financial statements.

Management is responsible for the integrity of the financial information. Internal control systems are designed and maintained to provide reasonable assurance that transactions are properly authorized, assets are safeguarded from loss or unauthorized use, and financial records are properly maintained to provide reliable accounting information for financial reporting purposes. KPMG LLP, independent external auditors, were appointed to perform an examination of the corporate and accounting records so as to express an opinion on the consolidated financial statements for the year ended December 31, 2006, and whether the consolidated financial statements are presented fairly in accordance with Canadian generally accepted accounting principles. The Auditors' Report to the shareholders is presented herein.

The Company's Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board exercises this responsibility through the Audit Committee. The Audit Committee meets regularly with management and the independent auditors to ensure that management's responsibilities are properly discharged, to review the consolidated financial statements and recommend that the consolidated financial statements be presented to the Board of Directors for approval. The external auditors have access to the Audit Committee without the presence of management.

Paul C. Starnino
President and Chief Executive Officer

April 12, 2007

Franco Civitarese
Vice President, Finance and Chief Financial Officer

April 12, 2007

Auditors' Report to the Shareholders

We have audited the consolidated balance sheets of E4 Energy Inc. as at December 31, 2006 and 2005 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and 2005 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants
Calgary, Canada

April 12, 2007

Consolidated Balance Sheets

As at December 31, *(in thousands of Canadian dollars)*	2006	2005
ASSETS		
Current		
Cash	$ 42	$ 809
Accounts receivable	4,863	3,617
Prepaid expenses and deposits	251	207
	5,156	4,633
Property, plant and equipment (Note 4)	54,640	39,599
Goodwill (Note 3)	8,509	8,509
	$ 68,305	$ 52,741
LIABILITIES		
Current		
Bank facility (Note 5)	$ 7,925	$ –
Accounts payable and accrued liabilities	6,880	5,394
Current portion of capital lease obligation	–	35
	14,805	5,429
Asset retirement obligation (Note 8)	1,613	1,079
Future income tax liability (Note 10)	4,784	5,787
	$ 21,202	$ 12,295
SHAREHOLDERS' EQUITY		
Share capital (Note 9 (b))	$ 47,464	$ 42,692
Contributed surplus (Note 9 (c))	3,371	1,532
Deficit	(3,732)	(3,778)
	47,103	40,446
	$ 68,305	$ 52,741

Commitments (Note 13)
Subsequent events (Note 15)

See accompanying notes to the consolidated financial statements.

On behalf of the Board of Directors:

Jim Brown
Director

Scott Saxberg
Director

Consolidated Statements of Operations and Deficit

Years ended December 31, *(in thousands of Canadian dollars, except per share amounts)*	2006	2005
Revenue		
Petroleum and natural gas	$ 15,486	$ 16,202
Royalties	(2,869)	(2,750)
	12,617	13,452
Expenses		
Operating	2,892	2,528
Transportation	487	828
General and administrative (Note 4)	2,433	2,685
Financing charges (Note 7)	460	684
Depletion, depreciation and accretion	9,433	7,363
Loss on asset retirement	–	97
Loss on disposal of equipment under capital lease	–	87
	$ 15,705	$ 14,272
Loss before taxes	(3,088)	(820)
Future income tax reduction	(2,969)	(1,124)
Net earnings (loss)	(119)	304
Deficit, beginning of year	(3,778)	(4,082)
Stock options settled for cash	165	–
Deficit, end of year	(3,732)	(3,778)
Earnings (loss) per share basic and diluted	$ (0.00)	$ 0.01

See accompanying notes to the consolidated financial statements.

Consolidated Statements of Cash Flows

Years ended December 31, *(in thousands of Canadian dollars)*	2006	2005
Cash provided by (used in):		
Operating activities		
Net earnings (loss)	$ (119)	$ 304
Items not affecting cash:		
Stock-based compensation	1,190	815
Finance charges	–	265
Depletion, depreciation and accretion	9,433	7,363
Loss on asset retirement	–	97
Loss on disposal of equipment under capital lease	–	87
Future income tax reduction	(2,969)	(1,124)
Asset retirement costs	(33)	(99)
Change in non-cash working capital (Note 11)	(655)	(2,014)
	6,847	5,694
Financing activities		
Proceeds from share issue, net of issue costs	6,506	9,608
Stock options exercised	108	637
Settlement of options	(168)	–
Issuance (repayment) of bank facility	7,925	(5,087)
Repayment of subordinated notes	–	(2,000)
Repayment of capital lease obligation	(35)	(200)
	14,336	2,958
Investing activities		
Corporate acquisition	–	4,708
Property, plant and equipment additions, net of disposals	(22,798)	(10,645)
Proceeds from disposal of subsidiary	–	15
Change in non-cash working capital (Note11)	848	(1,921)
	(21,950)	(7,843)
Change in cash	(767)	809
Cash, beginning of year	809	–
Cash, end of year	$ 42	$ 809
Supplemental cash flow information (Note 11)		

See accompanying notes to the consolidated financial statements.

Notes to the Consolidated Financial Statements

For the years ended December 31, 2006 and 2005

1. INCORPORATION AND NATURE OF OPERATIONS

Naneco Minerals Ltd. was continued under the laws of the Province of Alberta and changed its name to Southpoint Resources Ltd. on February 6, 2002. Southpoint at that time refocused its efforts to the exploration and development of petroleum and natural gas in western Canada. On August 23, 2005, in conjunction with the business combination discussed in Note 3, Southpoint changed its name to E4 Energy Inc. ("E4" or "the Company"). E4 is involved in the exploration, development and production of petroleum and natural gas in Alberta and British Columbia.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The financial statements are stated in Canadian dollars and have been prepared in accordance with Canadian generally accepted accounting principles. The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

Joint Operations

Substantially all of the exploration, development and production activities are conducted jointly with others and accordingly, the Company only reflects its proportionate interest in such activities.

Measurement Uncertainty

The amounts recorded for depletion and depreciation of petroleum and natural gas property, plant and equipment and the provision for asset retirement obligations are based on estimates. The cost recovery ceiling test is based on estimates of reserves, production rates, petroleum and natural gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be material.

Petroleum and Natural Gas Properties

The Company follows the full-cost method of accounting for petroleum and natural gas operations, whereby all costs related to the acquisition, exploration and development of petroleum and natural gas reserves are capitalized. Such costs include lease acquisition costs, geological and geophysical costs, carrying charges of non-producing properties, costs of drilling both productive and non-productive wells, the cost of petroleum and natural gas production equipment and overhead charges related to exploration and development activities.

Petroleum and natural gas assets are evaluated at least annually to determine that the costs are recoverable and do not exceed the fair value of the properties. The costs are assessed to be recoverable if the sum of the undiscounted cash flows expected from the production of proved reserves and the cost of unproved properties, net of impairments, exceeds the carrying value of the petroleum and natural gas assets. If the carrying value of the petroleum and natural gas assets is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying value exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves and the lower of cost and market of unproved properties. The cash flows are estimated using the future product prices and costs and are discounted using the risk-free rate.

Proceeds from the disposition of petroleum and natural gas properties are applied against capitalized costs except for dispositions that would change the rate of depletion and depreciation by 20 percent or more, in which case a gain or loss would be recorded.

Depletion and Depreciation

Capitalized costs, together with estimated future capital and retirement costs associated with proved reserves, are depleted and depreciated using the unit-of-production method based on estimated gross proved reserves of petroleum and natural gas as determined by independent engineers. For purposes of this calculation, reserves and production are converted to equivalent units of oil based on relative energy content of six thousand cubic feet of natural gas to one barrel of oil. Costs of significant unproved properties, net of impairments, are excluded from the depletion and depreciation calculation.

Asset Retirement Obligations

The fair values of asset retirement obligations related to long-lived assets are recognized as a liability in the period in which they are incurred. Retirement costs equal to the fair value of the asset retirement obligations are capitalized as part of the cost of the associated long-lived assets. Subsequent to the initial recognition, the obligation is adjusted each period to reflect the passage of time (accretion) and changes in the estimated cash flows underlying the obligation.

Revenue Recognition

Revenues from the sale of petroleum and natural gas are recorded when title passes to an external party.

Income Taxes

The Company follows the liability method of accounting for income taxes. Temporary differences arising from the differences between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax assets or liabilities. Future income tax assets or liabilities are calculated using tax rates anticipated to apply in the periods that the temporary differences are expected to reverse.

Stock-based Compensation

The Company applies the fair value method of accounting to all equity-classified stock-based compensation arrangements for both employees and non-employees. Compensation costs of equity-classified awards to employees are measured at fair value at the grant date and recognized over their vesting period with a corresponding increase to contributed surplus. Compensation costs of equity-classified awards to non-employees are initially measured at fair value, and periodically remeasured to fair value until the non-employee's performance is complete, and recognized over their vesting period with a corresponding increase to contributed surplus. Upon the exercise of the award, consideration received together with the amount previously recognized in contributed surplus is recorded as an increase to share capital. The Company accounts for forfeitures as they occur.

Goodwill

Goodwill is recognized on corporate acquisitions when the total purchase price exceeds the fair value of the net identifiable assets of the acquired company. Goodwill is tested for impairment on an annual basis in the fourth quarter. If indications of impairment are present, a loss would be charged to earnings for the amount that the carrying value of goodwill exceeds its fair value.

Flow-through Shares

When flow-through shares are issued the proceeds are used to fund qualifying exploration and development expenditures within a defined time period and are renounced to investors in accordance with tax legislation. Share capital is reduced and the future income tax liability is increased by the estimated future income tax cost of the renounced tax deductions when the renouncement is made.

Per Share Amounts

Basic per share amounts are computed using the weighted average number of common shares outstanding during the reporting period. Diluted per share amounts are calculated using the treasury stock method, which assumes that any proceeds from the exercise of stock options in addition to the unrecognized amount of stock-based compensation costs are used to purchase common shares of the Company at the average market price during the reporting period.

3. BUSINESS COMBINATION

On August 23, 2005, E4 acquired all of the common shares of P3 Energy Ltd. ("P3"), a private oil and gas company, pursuant to an Amalgamation Agreement (the "Agreement"). The P3 shareholders received one E4 common share for each of the 10,779,600 P3 common shares formerly held by them. The shares issued to P3 shareholders were valued at $1.31 per share, which was the five-day weighted average price of E4 shares prior to announcing this transaction, net of implied issue costs. In addition, the P3 directors, officers and employees, who continue to provide service to the Company, received one E4 stock option for each of the 623,000 P3 stock options formerly held by them at the same terms as the original P3 stock options. The acquisition date fair value of the replacement E4 stock options is $843,986. The earned portion of the replacement option fair value has been recognized as part of the purchase price consideration with the remainder to be amortized as stock-based compensation over the remaining service period. The acquisition of P3 was accounted for using the purchase method of accounting. The results of operations of P3 have been included in the consolidated financial statements from the date of acquisition. The following table summarizes the purchase price allocation:

($ thousands)	
Consideration:	
Common shares	13,415
Stock options	148
Transaction costs	183
Total	13,746
Net assets acquired:	
Cash	4,891
Working capital deficit	(381)
Property, plant and equipment	6,042
Goodwill (without tax basis)	6,197
Asset retirement obligation	(57)
Future income tax liability	(2,946)
Total	13,746

4. PROPERTY, PLANT AND EQUIPMENT

($ thousands)	2006	2005
Petroleum and natural gas properties	82,299	57,938
Accumulated depletion and depreciation	(27,659)	(18,339)
Property, plant and equipment, net	54,640	39,599

During the year ended December 31, 2006, the Company capitalized $1.6 million of general and administrative costs (2005 – $0.7 million) related to exploration and development activities.

The calculation of 2006 depletion and depreciation included an estimated $5.0 million (2005 – $0.6 million) for future development and associated retirement costs associated with proved reserves and excluded $7.2 million (2005 – $3.6 million) for the estimated value of unproved properties.

The prices used in the ceiling test evaluation of the Company's oil and natural gas assets are summarized in the following chart. Based on these assumptions, the undiscounted value of future net revenues from the Company's estimated proved reserves exceeded the carrying value of property, plant and equipment as at December 31, 2006.

Crude Oil and Natural Gas

	West Texas Intermediate (Cdn$/bbl)[1]	Company price per reserve report (Cdn$/bbl)	AECO Gas price (Cdn$/mmbtu)	Company price per reserve report (Cdn$/mcf)
2007	70.11	59.60	7.33	6.94
2008	68.97	59.20	7.91	7.58
2009	68.97	59.47	7.89	7.59
2010	66.67	57.55	7.87	7.58
2011	64.37	55.69	8.02	7.73
2012	65.66	57.47	8.19	7.95
2013	66.97	59.13	8.35	8.16
2014	68.31	61.66	8.52	8.44
2015	69.67	63.74	8.69	8.74
2016	71.07	67.91	8.86	8.94
Thereafter [2]	2.0%	2.0%	2.0%	2.0%

Future prices incorporated a $0.87 US/Cdn exchange rate

Percentage change of 2.0% represents the change in future prices each year after 2017 to the end of the reserve life.

5. BANK FACILITY

The Company has an $18 million revolving term demand credit facility with a Canadian chartered bank. The credit facility provides that advances may be made by way of direct advances, bankers' acceptances or letters of guarantee. Direct advances bear interest at the bank's prime lending rate plus 0.125 percent. The credit facility is secured by a $50 million demand debenture secured by a first floating charge on all assets and a general assignment of book debts. The $18 million borrowing base is subject to an annual review by the bank, with the next review expecting completion by late May 2007.

6. SUBORDINATED NOTES AND WARRANTS

On December 17, 2004, the Company issued subordinated notes in the amount of $2 million due in 18 months from the date of issuance that bore interest at a rate of 11 percent per annum. The subordinated notes carried one half of a detachable warrant for each $1.50 of principal with each whole warrant entitling the holder to acquire one common share of the Company at a price of $1.50 per share for a period of 18 months. The proceeds were allocated to the liability component (subordinated notes) and equity component (detachable warrants). The resulting discount on the notes of $0.3 million was being amortized over the term of the loan. In 2005, the subordinated notes were settled early at their face amount of $2 million resulting in a loss of $0.1 million. All warrants associated with these subordinated notes expired on June 17, 2006.

7. FINANCING CHARGES

Financing charges are comprised of the following:

Year ended December 31, *($ thousands)*	2006	2005
Interest expense	460	420
Subordinated note finance change	–	117
Loss on early retirement of subordinated note	–	147
Total	460	684

8. ASSET RETIREMENT OBLIGATIONS

The total future asset retirement obligation was estimated based on the Company's net ownership interest in all wells and facilities, the estimated costs to abandon and reclaim the wells and facilities and the estimated timing of the costs to be incurred in future periods. The total undiscounted inflation-adjusted amount of the estimated cash flows required to settle the asset retirement obligations is approximately $2.4 million which will be incurred over the next 23 years. A credit-adjusted risk-free rate of 8 percent was used to calculate the fair value of the asset retirement obligations. The following reconciles the Company's asset retirement obligations:

Year ended December 31, *($ thousands)*	2006	2005
Balance, beginning of period	1,079	657
Liabilities incurred	327	111
Liabilities acquired on business combination	–	57
Liabilities settled	(33)	(2)
Revisions	127	184
Accretion expense	113	72
Balance, end of year	1,613	1,079

Notes to the Consolidated Financial Statements

9. SHARE CAPITAL

a) Authorized

Unlimited number of common shares.

b) Issued and Outstanding

Common Shares

	2006	
	Shares	Amount *($ thousands)*
Balance, beginning of year	38,671,338	$ 42,420
Flow-through common shares issued for cash	3,889,000	7,000
Exercise of stock options	83,334	142
Share issue costs, net of tax		(344)
Tax effect on flow-through shares renounced		(1,754)
Balance, end of year	42,643,672	47,464
Balance warrants – December 31, 2005	666,667	272
Warrants expired on June 17, 2006 (Note 6)	(666,667)	(272)
Share Capital – Total		$ 47,464

	2005	
	Shares	Amount *($ thousands)*
Balance, beginning of year	22,577,404	$ 18,813
Common shares issued for cash	2,662,000	5,058
Flow-through common shares issued for cash	2,129,000	5,216
Issued on acquisition of P3	10,779,600	13,415
Exercise of stock options	523,334	777
Share issue costs, net of tax		(442)
Tax effect of flow-through shares renounced		(417)
Balance, end of year	38,671,338	42,420
Balance warrants – December 31, 2005 (Note 6)	666,667	272
Share Capital – Total		$ 42,692

c) Contributed Surplus

Contributed Surplus Continuity:

($ thousands)	2006 Amount	2005 Amount
Balance, beginning of year	1,532	441
Stock-based compensation	1,935	1,082
Stock-based compensation on acquisition of P3 (Note 3)	–	148
Cash settlement of stock options	(334)	–
Stock options exercised	(34)	(139)
Warrants expired	272	–
Balance, end of year	3,371	1,532

d) Flow-through Shares

On October 20, 2005, the Company issued 2,129,000 flow-through common shares at a price of $2.45 per share for gross proceeds of $5.2 million. These expenditures were renounced to investors of this financing in 2005. Under the terms of the flow-through share agreement, the Company was committed to spend the gross proceeds on qualifying exploration expenditures prior to December 31, 2006. This commitment was fulfilled during 2006.

Prior to the acquisition date of P3 on August 23, 2005 (Note 3), P3 issued flow-through common shares for gross proceeds of $3.6 million. These expenditures were renounced to investors of this financing in 2005. As a result of the business acquisition, the Company had assumed the obligation to spend the gross proceeds on qualifying exploration and development expenditures prior to December 31, 2006. This commitment was fulfilled during 2006.

On November 30, 2006, the Company issued 3,889,000 flow-through common shares at a price of $1.80 per share for gross proceeds of $7.0 million. These expenditures were renounced to investors of this financing in 2006. Under the terms of the flow-through share agreement, the Company is committed to spend the gross proceeds on qualifying exploration expenditures prior to December 31, 2007. As at December 31, 2006, the Company had incurred approximately $0.6 million of qualifying expenditures.

e) Stock Options

Under the Company's stock option plan, the Company may grant options to its directors, officers, employees and consultants to purchase common shares at a fixed price not less than their fair market value on the day preceding the grant date. The options vest at a rate of one-third on the six-month anniversary of the date of grant and a further one-third on each of the one-year and two-year anniversaries from the date of grant. The option's maximum term is five years. The following table sets forth a reconciliation of the stock option plan activity.

2006	Options	Weighted Average Exercise Price $
Balance, beginning of year	2,748,335	1.48
Granted	1,125,000	1.75
Settled	(550,001)	1.44
Forfeited	(22,667)	1.75
Expired	(8,333)	1.75
Exercised	(83,334)	1.30
Balance, end of year	3,209,000	1.58
Number of options exercisable	1,756,330	1.54

2005	Options	Weighted Average Exercise Price $
Balance, beginning of year	1,831,400	1.34
Granted	1,940,000	1.49
Forfeited	(499,731)	1.36
Exercised	(523,334)	1.22
Balance, end of year	2,748,335	1.48
Number of options exercisable	972,669	1.32

The following table summarizes stock options outstanding and exercisable under the plan at December 31, 2006.

	Options outstanding			Options exercisable	
Range of exercise price	Number outstanding at period end	Weighted average remaining contractual life (years)	Weighted average exercise price	Number exercisable at period end	Weighted average exercise price
$1.00 to $1.49	928,000	3.11	1.10	618,668	1.10
$1.50 to $1.82	2,281,000	3.81	1.78	1,137,662	1.78
	3,209,000	3.61	1.58	1,756,330	1.54

The fair value of options granted during the period was estimated on the date of grant using the Black-Scholes option pricing model with weighted average assumptions and resulting values for grants as follows:

Weighted average assumptions and results	2006	2005
Risk-free interest rate (%)	3.90	3.64
Expected life (years)	5.00	5.00
Expected volatility (%)	65.0	74.4
Fair value of options	$ 1.01	$ 1.18

The Company in 2006 recognized, $1.2 million of stock-based compensation expense (2005 – $0.8 million). In addition, the Company capitalized $0.8 million of stock-based compensation expense in 2006 (2005 – $0.3 million). The expensed portion of stock-based compensation is reflected on the Company's consolidated statement of operations.

In January 2006, the Company settled and cancelled an aggregate of 550,001 outstanding vested stock options with a weighted average strike price of $1.44, with its former employees. Total proceeds of $168,167 were paid to the former employees with respect to this settlement. The excess of the grant date fair value over the cash settlement has been recorded as a decrease to the deficit.

f) Share Purchase Loan

In conjunction with the flow-through share issue on December 30, 2004, the Company provided a share purchase loan in the amount of $48,000 to an employee secured by 30,968 common shares. As part of the business combination in Note 3 above, the share purchase loan was offset with the accrued liability for severance for this employee.

g) Earnings (Loss) Per Share

The weighted average number of common shares outstanding during the year ended December 31, 2006 used in computing both basic and fully diluted loss per share was 39,095,077. Excluded from the fully diluted weighted average number of common shares outstanding at December 31, 2006 were 2,708,667 stock options that were anti-dilutive. The weighted average number of common shares outstanding during the year ended December 31, 2005 was 27,557,342, which was used in computing basic earnings per share. In calculating diluted earnings per share for the year ended December 31, 2005, 65,538 shares were added to the weighted average number of basic common shares outstanding. Excluded from the fully diluted weighted average number of common shares outstanding at December 31, 2005 were 2,983,068 stock options that were anti-dilutive.

10. FUTURE INCOME TAXES

The provision for future income taxes in the statements of earnings and retained earnings reflects an effective tax rate, which differs from the expected statutory tax rate. Differences were accounted for as follows:

($ thousands)	2006	2005
Net loss before income taxes	(3,089)	(820)
Statutory income tax rate	35.1%	38.1%
Expected income taxes	(1,084)	(312)
Add (deduct):		
Non-deductible Crown charges	218	580
Resource allowance	(257)	(558)
Stock-based compensation	418	400
Change in tax rates	(829)	(24)
Change in valuation allowance	(1,436)	(1,344)
Other	1	134
Future income tax reduction	(2,969)	(1,124)

The future income tax liability at December 31, 2006 and 2005 is comprised of the tax effect of temporary differences as follows:

($ thousands)	2006	2005
Property, plant and equipment	(6,623)	(7,541)
Asset retirement obligations	473	363
Losses	1,107	1,186
Share issue costs	259	205
Future income tax liability	(4,784)	(5,787)

Of the $1.1 million in losses in the table above, $0.4 million will expire by 2010 and $0.4 million will expire by 2015.

11. SUPPLEMENTAL CASH FLOW INFORMATION

a) Increase (Decrease) in Non-cash Working Capital Items

($ thousands)	Year ended December 31, 2006	2005
Change in non-cash working capital:		
Accounts receivable	1,246	174
Prepaid expenses and deposits	45	63
Accounts payable and accrued liabilities	(1,484)	(4,163)
Working capital of subsidiary sold	–	(9)
	(193)	(3,935)
Changes in non-cash working capital related to:		
Operating activities	655	(2,014)
Investing activities	(848)	(1,921
	(193)	(3,935)

b) Interest

($ thousands)	Year ended December 31, 2006	2005
Interest paid	418	420

12. FINANCIAL INSTRUMENTS

Fair value of financial assets

Cash, accounts receivable, deposits, accounts payable and accrued liabilities, bank facility and capital lease obligations constitute the Company's financial instruments. Based on their short-term maturities or market rates of interest, the carrying values of these financial instruments approximate their fair values at December 31, 2006 and 2005.

Credit risk

The Company's petroleum and natural gas production is marketed to a variety of purchasers to mitigate such credit risk.

Accounts receivable are with customers and joint venture partners in the petroleum and natural gas business under normal industry sale and payment terms and are subject to normal industry credit risks. The Company routinely assesses the financial strength of its customers. The Company generally extends unsecured credit to customers and, therefore, the collection of accounts receivable may be affected by changes in economic or other conditions. Management believes the risk is mitigated by the size and reputation of the companies to which credit has been extended. The Company has not experienced any material credit loss in the collection of accounts receivable.

Interest rate risk

The Company is exposed to interest rate risk to the extent that changes in market interest rates will impact the Company's debts that have a floating interest rate. The Company had no interest rate swaps or hedges at December 31, 2006.

13. COMMITMENTS

The Company is committed to incur approximately $6.4 million prior to December 31, 2007 on qualifying exploration and development expenditures relating to the flow-through common share financing of November 30, 2006 (see Note 10 (d)).

At December 31, 2006, the Company has committed to certain payments over the next two years as follows:

Office Rental

($ thousands)	2007	2008
	189	142

In addition to these amounts, the Company is responsible for its proportionate share of operating costs pertaining to the noted office facilities, which are periodically reviewed and determined by the landlord.

14. RELATED-PARTY TRANSACTIONS

A director of the Company is a partner at a law firm that provides legal services to the Company. During the year ended December 31, 2006, the Company paid a total of $0.05 million to this firm for legal fees and disbursements. An additional amount of $0.04 million was accrued at December 31, 2006 and paid in 2007. During the year ended December 31, 2005, the Company paid and accrued a total of $0.1 million to the same law firm.

15. SUBSEQUENT EVENTS

On January 31, 2007, the Company entered into a firm fixed price agreement with one of its natural gas purchasers. The term of the agreement is such that the first 1,500 gigajoules per day from the Company's McMahon receipt station will have a fixed price of $7.40 per gigajoule. This contract commences on April 1, 2007 and continues until October 31, 2007.

E4 Energy Inc.

STOCK EXCHANGE LISTING

TSX Venture Exchange
Symbol: EFE.V

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Graham Cormack, P. Eng.
Vice President, Engineering and Operations

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ABBREVIATIONS

bbls	barrels
boe	barrels of oil equivalent
boe/d	barrels of oil equivalent per day
mboe	thousand barrels of oil equivalent
mcf	thousand cubic feet
mcf/d	thousand cubic feet per day
mmbtu	million British thermal units
mmcf	million cubic feet
NGL	natural gas liquids
NYMEX	New York Mercantile Exchange
W.I.	working interest
W.T.I.	West Texas Intermediate

Printed in Canada
Designed and produced by Merlin Edge Inc.


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